ADEPT
Socioeconomic Commentaries

May-September 2004

EU enlargement: lessons for the Republic of Moldova
Iurie Gotisan, 5 May 2004

As of May 1, ten new countries that had successfully passed the "admission test" joined EU and became full-rights members. It wouldn't be long until Poland, Lithuania, Latvia, Estonia, Hungary, Czech Republic, Malta, Cyprus and Slovakia would enjoy the benefits of the marriage between East and West planned ahead a decade ago. The enlarged EU has set a rather ambitious task to become in five years the most competitive world power fully integrated politically and economically, capable of influencing other actors on the international arena.

In this respect, given Moldova's efforts to join EU many analysts wonder what impact would enlargement have on Moldovan economy. To begin with, there is the risk that the trade would drop sharply as would revenues from exports. And this largely due to Moldovan goods being eliminated from the EU market and tariff barriers in trading with the new member states. Another negative impact might be the price hike on goods imported from those countries, as they would align them to current EU standards. As a result, weak and non-competitive companies in Moldova run the risk of being excluded from the market that would inevitably boost unemployment and crime. Finally, free movement of labour would be quiet onerous to achieve in new members as some of them face a fierce shortage of workplaces and high unemployment rates.

Albeit it stepped on its independence path at the same time with Baltic States that were probably integrated in the soviet economic system to a larger extend, Moldova failed to capitalize on its political independence so as to secure its economic independence and is still lagging behind in as far as accession to EU is concerned for quite a while now. That "while" cost Moldova investments worth million euros that would go to countries boasting a better business climate and playing by the rules. That is not the case of Moldova, which according to Moldova-watchers is among the poorest and most corrupt countries in Europe. It has the lowest average annual income per capita worth 230 euro per capita and an average wage per hour of only 0.3 euro. Poverty has reached scary levels with 40% of the population under the minimal subsistence level. Not to mention that the country is struggling to have its Poverty Reduction Strategy.

How was it possible for countries that had stood equal chances to be so far apart? Whose fault was it that Moldova is lagging far behind countries like Estonia with a population three times smaller than Moldova's and far scarcer resources? Economists and politicians alike agree that first and foremost political elite is to be blamed, which acted more like an obstructer than promoter of reforms. Nothing and nobody could guarantee that reforms are irreversible in this country, as it still hasn't got rid of duality in foreign policy. Situated on the crossroads of two superpowers Moscow and Brussels, Moldova failed to understand that staying in two boats at the same time has led to the division of the country.

Previous governments failed to come up with a clear and coherent strategy, not to speak of a viable one. Political will was lacking, in the hope that things would just settle by themselves, without affecting rulers' positions. Economic strategies, if one may call them so, bolstered inefficiency and shadow economy rather than welfare, productivity and investments. Governments were more concerned with promoting exaggeratedly protective social policies having no financial coverage that were eroding state budget, instead of encouraging businesses to invest so as to open up new jobs.

Lack of political will has affected the reform in every sense, i.e. the state still has to privatize Moldtelecom, North and North-West electricity distribution networks and many other wineries and tobacco factories. Infrastructure is a mess; pro forma legal framework, whereas investments amount only to 3% of the GDP, which is far less than in Poland, Czech Republic or Hungary boasting a steady 40%. Clearly a country as small and as poor as the Republic of Moldova is with such a complex, unstable and ambiguous legal framework, hardly seems luring to the foreign capital.

When it comes to foreign investments Moldova has lost so far great many opportunities. There were times when those nostalgic for the good old times stood strongly "We are not selling our country!", at times when Latvia or Estonia were selling state enterprises to such world giants as Pepsi or General Electric. Moldovan businessmen and managers agree that attitude towards foreign investors, failure of investment programs in infrastructure, lack of measures aimed at boosting successful sectors of economy instead of subsidizing unsuccessful ones, and legal chaos are among the major factors that kept Moldova far from Europe. Great many businessmen point that shortage of investments is largely due to poor infrastructure. Differences in mentality and culture between Moldova and new EU members have only highlighted the huge gap between Moldova and Western Europe.

Apparently, rules have been set to bring us closer to European standards, however few observed them. Indigenous businesses are still treated differently by authorities than their foreign counterparts, and that largely because money is the main incentive in decision making. Under given circumstances, Government may want to provide a level playing field for all players, start showing "yellow cards" to those breaking the rules and stop tolerating high rank officials doing murky bargains at their own will.

State owned enterprises accounting for as much as 65% and is kept afloat by subsidies and bad credits, on top of that Moldova is under the watchful eye of Council of Europe for lack of democratic practices. Political and social instability that dominated the country in the last decade coupled with lack of knowledge and skills in running a national economy are those critical factors that thwarted a breakthrough in economy.

At the same time, it should be clear that state institutions are not solely responsible for that state of affairs. They are week, inefficient, scarce of financial and human resources. Civil society has its own share of responsibility in that. However, as the pioneers of economic liberalism showed private initiative is the fundamental condition of welfare in society. Where the state is impotent, corrupt and incapable, one should take his future on his own hands. Therefore, more actions, persistence and personal courage - those are the ingredients of success for our society that in the long term would bring us the family of European nations.

Domestic foreign exchange market: on-going volatility
Iurie Gotisan, 12 May 2004

Democracy and governing in Moldova
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In the last two weeks Moldova Lei constantly appreciated against USD by 11.2% and reached its highest in the last five years being traded over 11,5 Lei per USD. According to the National Bank experts and economy-watchers the fluctuations are largely due to strong supply of foreign currency, mainly money sent home by Moldovans working abroad.

At the same time, recent evolutions on the domestic foreign exchange market, in particular price hike (implicitly inflation rate that has reached 3% in the first quarter of 2004) amidst considerable appreciation of the Lei, signals major pitfalls for National Bank. Apparently, appreciation in real terms of the exchange rate is an outcome of the National Bank's monetary policy focusing on strict control of the monetary base (M0), i.e. cash in circulation and money banks hold on the Central Bank account.

Of course, foreign exchange market, as are other markets, is regulated by economic rules, respectively, exchange rate is shaped demand and supply on the market. It is known for a fact that foreign exchange markets are heavily influenced by two factors: trade deficit that needs to be financed and capital flows invested in economy. Then, what's the impact of exchange rate on the economic realities in the Republic of Moldova from the perspective of those two factors?

For a start, foreign exchange policy announced and employed by the National Bank of the Republic of Moldova allowed for a real appreciation of the Leu, which affected the trade balance. That this policy does not help keeping inflation under control is yet another story. Another major pitfall, for Moldova, which is facing a huge external pressure, is the appreciation of the real exchange rate. That is, currency appreciation discourages exports and boosts imports, which as a result propels trade deficit further upwards. According to the latest press releases issued by the National Bank, trade balance deficit has reached 107 million USD in the first quarter of the year.

To diminish strong fluctuations of the exchange rate Moldovan economists recommend establishing Foreign Exchange Council, that is an exchange rate of the national currency against a single reference foreign currency (in contrast to a Central Bank that may issue money at any time, Monetary Council issues national currency only in exchange for assets in reserve, that is, foreign currency reserves of the central bank). A fixed exchange rate would protect domestic foreign exchange market from negative evolutions on the international financial markets. In a small and open economy as Moldovan is, heavily reliant on foreign markets (Moldova's dependence on foreign trade exceeds 70% of the GDP), fluctuating exchange rate wields heavy inflationist pressure that may at any time lead to disastrous effects in economy. Bulgaria established a Foreign Exchange Council in 1997 as a cornerstone of an ambitious program of stabilizing inflation, which dropped by 580% in 1997 accounting for less that 1% in 1998.

Ongoing negative balance of the current account stems from the persisting swelling trade balance deficits of the Republic of Moldova amounting to 408 m USD in 2002 and 666 m in 2003. If we are to consider private transfers made by Moldovan citizens working abroad that according to Minister of Economy Marian Lupu reached 1 billion USD throughout 2002-2003, they practically covered for trade balance for the last two years. However, albeit constantly swelling, foreign currency transfers that are so much praised by media outlets as being very important and able to cover for the amount of trade deficit, they are still an unreliable source of funding. In their turn, foreign direct investments are easily reversed, not to speak of the instability of the "hot money", i.e. speculative flows on the foreign exchange market. Having said that, at the first glance financing trade balance via autonomous flows seems less certain.

Secondly, in the structure of the current account transfers from abroad, especially from citizens working abroad are far from diminishing trade balance deficit. To put it differently, albeit these are still considerable they loose grounds due to growing imports over to exports. In this respect, negative trade balance in the first quarter of the year rose to 34% or 28 m USD over similar period last year. Finally, one may not speak of a foreign direct investments flow into Moldova able to automatically finance the swelling trade deficit. Therefore, foreign direct investments placed in Moldova throughout 2003 amounted only to around 70 m USD.

Finally, amidst nominal appreciation of the Lei against USD, commercial banks would not be willing to make placements in foreign currency and as a result would have to diminish the amount of credits granted to the real economy sector, thereby propelling interest rates further upwards. Being affected by high interest rates, economy would attract only short-term capital that might lead to a sharp appreciation of Lei in real terms, thereby dropping export revenues and swelling trade balance deficit.

One may argue that swelling interest rates would lure foreign capital that would automatically increase the supply of foreign currency and would reduce the monetary base to its initial state. Unfortunately, though, realities of Moldovan economy make us consider the opposite scenario, especially given state's deficient investment policy. The type of capital that might be lured by the swelling interest rates would most certainly be a speculative one, ready to exit the country at the first sign of risk. Therefore, it may well happen that we would end up in a vicious circle that might as well lead to massive capital outflows.

It is not certain how long would National Bank be able to support the financial pyramid that is on the verge of collapse. Nevertheless, let us hope that autumn 1998 was the greatest ill we had to experience.

Despite the constant economic growth, people think they are poorer
Iurie Gotisan, 2 June 2004

Democracy and governing in Moldova
e-journal, II year, no. 31, 2 June 2004

1. Poverty Reduction and Economic Growth Strategy (PRSP) approved

On May 19 Government approved PRSP, a document including social economic policies to be implemented over 2004-2006 to ensure sustainable economic growth and reduce poverty. In the eyes of many Republic of Moldova is the poorest country in Europe. Strategy indicates that despite the overall 21.6% GDP growth over the last three years, average monthly salary rose by 70.1% and average monthly pension by 93%, poverty still remains to be a major issue. Moreover, it is estimated that around 40% of the population live below subsistence level, whereas 35-40% of the working population has left the country in search for a decent earning.

On May 25, the final PRSP version was submitted for the evaluation and final approval of the World Bank. Authorities expect WB to approve the document by July so that it becomes operational. Noteworthy, PRSP has been developed for four years. In 2000 WB Governing Board approved the preliminary PRSP developed by Braghis Government. After Braghis Government was ousted in spring 2001, the document was revised and later approved in 2002. However, after civil society and international organisations voiced their lingering concerns with regard to the quality of the document, the period of working out on the document was extended for another year.

Furthermore, PRSP would be also submitted to USAID, UNDP, CIDA, other partner agencies that would bring their technical assistance priorities in line with the strategy. Chisinau is now considering how the Parliament would approve PRSP, as a law or as a resolution. Experts believe the document should not have the status of the law.

Being a guideline for future technical assistance programs PRSP would secure the most needed and advantageous foreign aid. A special attention shall be given to the feasibility and clarity of the priority actions developed by the Government, as well as to the monitoring mechanism that would allow for on-going improvement of the document.

Noteworthy, the current PRSP version is of a higher quality than the previous drafts and is among the best similar documents developed in Moldova since independence. However, experts point to certain shortcomings, some of which would be addressed upon public debates over the document. According to IMF and WB standards the Governments itself should identify and acknowledge the strengths and weaknesses of Poverty Reduction Strategies as well as risk factors.

2. Poverty is becoming a major problem for more and more people

Implementing PRSP is paramount. Great many Moldovan citizens, around 90% consider themselves poor according to the findings of an opinion poll commissioned by Institute for Public Policies and conducted by CIVIS in April-May 2004 at the order of. Interviewees had to assess their welfare on a scale of 1 to 10, "poor" and "rich" respectively. Almost 10% rated their welfare at 1 point thus considering themselves "poor", 13.3% rated it at 2 points, 21.9% at 3 points, 21.3% at 4 points, and 24.6% at 5. Only 9.2% rated their welfare from 6 to 8 points. What is striking is that none of the interviewees rated his/her welfare at 9 or 10 points.

At the same time, 42.8% of the interviewed claim current income of their family is not sufficient even "for the essentials of life", while 40% - "only for essentials of life". Moreover, 86.8% of the interviewed say they are not satisfied with their wage and only 8.8% are "quite happy" or "very happy" with it. As compared to 2003 there was registered a significant increase in people's fear of price hike 50% (a 23% increase over last year), of poverty 64% (11% increase over last year), and future of the children 52% (8% increase).

35.8% believe life in Moldova would get better or slightly better in one year, 25.5% believe nothing would change in one year. Still 43.2% of the interviewed say this year economic situation is "better" or "slightly better", whereas 34.7% believe it is the same, with only 8.4% being satisfied with the current state of affairs, while 47.6% are not quite satisfied or not satisfied at all. Persons interviewed said that to improve the socio-economic situation in the country it is necessary to improve law enforcement, increase the role of the state in administering economy, attract more foreign investments, boost industrial output and fight corruption.

Noteworthy, many people live from subsistence farming. People judge economy by the money in their pockets. Last opinion poll registered a significant increase in the unhappy or unsatisfied ones. Almost 40% believe economic situation worsened after the incumbent Government had come to power. The following factors that worsened the situation are cited: drop of income, price hike and no job.

Opinion poll also indicates that the great majority of Moldovans wish for a more homogenous society without any huge inequalities in income. It is very important how people perceive social injustice, as any increase in inequality brings about a decrease in solidarity and trust among members of the society. The poll also shows that 80% view Moldovan society as highly unjust, with great many poor and a handful of extremely rich.

Employment is the Key Issue
Galina Selari, 16 June 2004

Democracy and governing in Moldova
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The economic growth, its quality, rate, parents and sustainability is one of the vexed question today. And it is widely discussed by politicians, economists and journalists. The issues of export-import, migrants' remittances and others are put on the discussion.

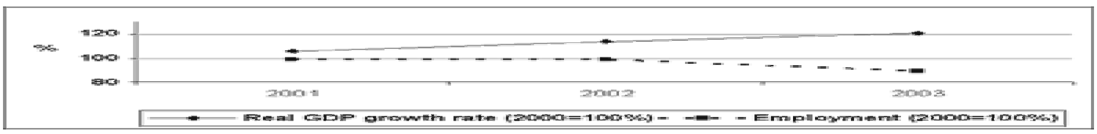
However, the *key question* - employment has remained in the shadow.

The problem of labour resources use remains very acute and that why it should be solved urgent.

Economic transformations and changes in ownership structure resulted in changes in labour relations and employment sphere. During the first phase of economic reforms the response of Moldovan labour market to sharp decrease in industrial output appeared as average *wage cut* but not as *release labour*. So, as compared with 1990, in 1996 the GDP dropped by 63%, amount of wage - by 80%, but the number of employed population - by 20% only. At the same time the king-size shadow economy was created and the unconcealed shadow employment without any legal background or labour contract was in blossom.

The fact that economic growth occurred in Moldova during the recent years came to 6-% on annual average has had no evident positive influence on labour market. It is a pity, but economic growth can't eliminate all social deformations by itself and to belief that it can make this is no more than illusion. And such illusions should be disappeared.

In fact, the sizable increase of production had not resulted in job growth but even more the number of employed persons slightly decreased and the number of unemployed went up.



But for all that even an employed person could be considered as semi-employed: in 2003 the average monthly wage size was only 34% above the *minimum* subsistence or enough to cover nearly 70% of minimal consumer budget.

Within certain limits this could be explained by underemployment: those who worked less than full time or are in unpaid vocation (about 5-6% of total employment) and those who work full time, but both the work and income is shared, i.e. ineffective use of labour force.

The shadow employment still exists either. It simply adjusted to new realities: now we have legal labour contracts, but often they have a formal character and as before based on the principle - *"as we will agree"*.

Such marginal forms of relations at the labour market have become rather stable. And, strictly speaking, there is no reason to believe that they will ever be eliminated in the foreseeable future.

It appears that this is exactly the price our market has paid over the decade of not-so-consequent reforms.

And here is another illusion: everything depends on investments; once funds are invested into economy, we will succeed in everything, the growth will become sustainable and the universal revival will begin, as well as all other kinds of grace.

There is no doubt that we need investments - labour force follows the production capital flow. And Moldova has been a visual proof of this during all last years. Almost every third family has now its "representative" abroad. In 2003, circa 280 thou of our compatriots worked abroad earning their living (Household Budget Survey data). Naturally, a gradual mental re-evaluation takes place: "work to live" rather than "live to work".

And a question arises - whether our labour market is ready for the investments inflow? There is no simple answer, unfortunately. A phenomenon has formed: stable unemployment coexists with the labor force deficit. Say, there is an excess of managers and jurists, while metalworkers and turners are needed. It turns out that workers of specific professions, specific qualification, specific skills are needed, rather than just workers. And the current labour market often falls behind the real needs of the economy.

The demographic forecasts are also distressing. It looks like 2003 was the last year of the population growth and the absolute number of persons able to work will decrease in the future. In 2010 labour resource growth will make up no more than 9 thou persons and in 2015 the negative growth is expected of 20 thou persons at least (the calculations are very approximate as the last population census was conducted in 1989). One could supplement this with the loss of workers from prolonged unemployment: a person loses qualification after about a year of involuntary idleness and unsuccessful search for work (now, the average period of unemployment in the country is 23 months). Moreover, there is an acute lack of persons who know to work in a workmanlike manner. The reason is obvious: neither employers, nor workers are ready for the full-fledged market relations.

A conclusion arises: the labour market is not ready for investments. Moreover, it is - in a certain sense - a hindrance to activization of investment processes. And if the market is not ready for investments, it is possible that they will not happen or will not yield the expected result.

What can and should the state do under such difficult conditions/ firstly, it should elaborate a complex programme of actions in the socio-labour sphere - a labour market concept and measures of its implementation, i.e. create an effective and civilized labour market in Moldova, which would operatively supply employers with the labour force of required qualification and workers - with the work and adequate wage.

So, with solving employment problem we will achieve both most important our goals: sustainable economic growth and poverty reduction.

Challenges faced by the National Bank
Iurie Gotisan, 30 June 2004

Democracy and governing in Moldova
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1. National Bank's monetary policy: achievements and impact

Undoubtedly, one may find Moldova's macroeconomic achievements (given the economic growth registered in the last three years) acceptable, as banking sector managed to steer away from a system crisis despite the difficulties it faced. Still, the country is not able to secure sustainable economic growth, reduce unemployment and keep inflation down. There are great many factors both at the macroeconomic level, i.e. structural deficiencies of Moldovan foreign sector of economy (exports, servicing foreign debt), as well as the microeconomic level, i.e. slow progress of enterprise restructuring, privatization, and institutional development in general; that account for such a state of affairs.

National Bank pursued a restrictive monetary policy throughout those years aimed at keeping prices stable, however that policy proved to be unfeasible, inconsistent and unable to keep inflation under control (National Bank has made its goal quite clear - to keep inflation under control, however 2003 it failed in its pursuit). Being under pressure, National Bank systematically provided credits to the "vulnerable" sectors as well as to commercial banks facing problems. Those were only some of the shortcomings of the NBM activity throughout those years. At times it directly funded public deficits albeit the move ran counter to its efforts to keep prices stable. It frequently has made wide-scale interventions on the foreign currency market (especially buying USD and Euro), which is yet another policy set to soar the monetary base and also boost inflation. For instance, 15.7% inflation rate registered in 2003 undercut NBM's great policy and has led some to the conclusion that Moldovan economy is ill fated.

At the end of May 2004 annualized inflation rate was estimated at 12% and some experts believe it is still set to soar. An eventual price hike in 2005 might be brought about by a tax cut both for legal and natural entities as scheduled by the Government for early 2005.

Usually, Governments are tempted to swell their ratings on the eve of elections by tax cuts and increase in the social sphere spending. However, such actions might boost the internal consumption, which in its turn might set the domestic debt and budget deficit to soar, onerous dilemma for the NBM. To enlarge and accrue funds to state budget revenues, at the recommendation of NBM, Government would probably raise customs taxes and tariffs for export-import operations (which account for 70% of the budget revenues). The move would probably serve a strong stimulus for importers and exporters alike to raise production price, respectively sale price, which in turn would affect inflation rate.

Therefore, NBM faces a double challenge in its monetary policy attempting to reduce inflation. Firstly, this policy mix should include a revenue policy and small budget deficits based on rigorous controls coupled with rationalization of public spending and financial discipline imposed at the company level. Huge deficits lead to high interest rates and require a more flexible monetary policy for counterbalance, however such a policy poses a number of difficulties for an open economy like Republic of Moldova is. Secondly, liquidity should be under control and strong inflationist expectations after years of "programmed inflation" should be ended. As long as there are no major changes in the monetary policy, either because of the lack of political will or lack of relevant institutions or infrastructure, it would be quite difficult to bring about a turnaround in the expectations.

2. Impact of NBM's policy on economy

Albeit a relative stability of the prices and exchange rates, there was no breakthrough in the financial or banking sector, which has led to a even higher financial dependence over foreign donors. NBM policy has had a contrary effect, i.e. holding back economic and investment activity. Because of still high interest rates, bank credits have become inaccessible for investment projects funding, while great many jobs were cut. On a short-term such a policy is acceptable, as the first risk any economy should address is that of inflation out of control. However, on the long-term, once a macroeconomic stabilization is achieved and once populations' inflationist expectations are hold back, keeping inflation down should no longer be a top goal in the macroeconomic policy, which should instead focus on economic growth and fighting unemployment.

NBM together with the Government are the key players responsible for establishing an attractive investment climate in Moldova. For instance, throughout 2003 investments in Moldova reached 58 million USD, two times less than in 2002. It represents only 13 USD per capita, not accounting for Transdnistria, whereas in Romania it amounted to 7 billion USD in 2003 that is almost 320 USD per capita. It is all-too-clear that via its policies National Bank stimulated capital outflow from Moldova. This specifically refers to the norms banning and limiting free exchange of Leu into other currencies. Secondly, interdictions were set on foreign currency in the companies' pay office and bank deposits. Thirdly, monitoring over foreign currency transactions was increased, namely foreign currency may not be hold on a current account for more than three days. And finally, a new procedure of notifying specialized bodies, prosecution in particular, on the amounts hold in the bank account. Undoubtedly, Moldova's economy and legal framework, including the investment climate are not the most luring ones, still the aforesaid NBM's actions are greatly accountable for the capital outflow. Why is the capital outflow such a critical factor? It is because when capital outflows it brings about such phenomena as: soaring unemployment, shut down of enterprises unable to stand fierce competition due to their obsolete technologies, lack of well paid jobs, devaluation of assets on financial and monetary market, state's inability to keep up its social promises and accrue revenues to the state budget, and most importantly country morphing into an economic cemetery. The future seems quite gloomy for the young generation, i.e. no jobs, leaving the country being the only solution left. And things seem to get worse and worse as there is no quick fix at hand.

In case the aforesaid issues were to be address efficiently, then all the aspects of economic policy would have to be synchronized, coupled with a fine-tuning of the agencies responsible for its enforcement. Until now the waters have been calm with the Government refraining from any spectacular moves and National Bank having a quiet usual performance. Handing those economic deficiencies would test Government and National Bank's ability to struck mutually beneficial agreements.

Echo of the bread crisis
Anatolii Gudym, 14 July 2004

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Many people still remember the troubles of the wheat and bread crisis of 2003: bad wheat harvest, protracted reaction of the Government, "bread mafia", abrupt increase (39.8% a year) of prices for bread, emergency actions of the Parliament, Government and economic units to import wheat. One as well could think the situation is under the control now. The Higher Security Council of the Republic of Moldova under the President V. Voronin examined the facts of the matter twice (February 28 and April 27, 2004) and "demanded the Government to take measures that would allow no more bread crises, to call those responsible to account and establish a strict control over economic units activating in this field" [1].

It should be mentioned though that the main indicator - prices for bread - stabilized in the first half of 2004 (% to the December of 2003) [2]:

	January	February	March	April	May	June
First grade bread	99,8	99,8	99,8	99,8	95,0	94,9
Second grade bread	100,2	100,1	100,1	100,2	97,0	96,6

And first of all this is beneficent for the poor (circa 40% of the population) that spend the major part of their incomes for food.

Sudden news

And all of a sudden, when nobody expected it, alarming information came from the "bread frontline" in July:

- mayors of some settlements (Cricova, Sinjera, Ciorescu) stated during a session of the Chisinau municipal council there are bread lines and deficiency of "cheap" bread whose main consumers are pensioners and poor families;
- Franzelutsa SA controlled by the state, the monopolist (about 90%) in the bread production in the municipality, despite the Government recommendations halved (down to 20% instead of 35-40%) production of "cheap" bread since its losses during May alone made up 1,6 mil MDL;
- The harvest has begun and the wheat producers (it is expected that the crop will be good of 700-800 thou tons) worry about its sale and price. While the Government promised that it "will announce terms of purchase of bread grain in the nearest future and intends to buy grain directly from producers for a price that would account for expenditures and revenues" [3]. The Ministry of Agriculture thinks that it will most likely be 1,8-2,0 MDL per kg of wheat;
- In the meantime, the neighboring Romania that also expects a good crop set a 25% customs duty on wheat, citing the need to protect its internal market from cheap grain from Moldova, Ukraine and Russia [4].

Actions of authorities

The bread crisis of 2003 that has endangered the country's food security, as it is well-known, has also seriously shaken the whole state machinery. Learning a lesson from the occurrence, the President, Parliament and Government took a series of urgent actions to regulate the situation in the bread and grain market. Among them were:

- decisions of the country's Higher Security Council to monitor the bread and grain market, take control of prices and importers to eliminate illegal schemes with participation of many intermediaries;
- the Parliament prolonged the term of exemption of VAT and customs duties concerning the wheat (as well as of rye, barley and corn seeds) import till September 1, 2004;
- the Government decreased prices for 10-12% on average since May 1, 2004, for bread produced by Franzelutsa SA (in November of 2003 the enterprise increased them by 46%). At the same time, a programme to prevent bankruptcy of this enterprise was elaborated through compensations of its grain purchases from the state reserve and restoration of lost circulating assets;
- the import was monitored; but instead of expected 115 thou tons of wheat there was imported in the first half of 2004 only 19,4 thou tons, but, on the other hand, a lot of flour - 46,2 thou tons; a tender was conducted (the winner is Moldova Druck SA) to deliver to Moldova 12,5 thou tons of wheat from Canada and Latin America at 164,0 USD per ton to Ilyichevsk (Odessa) port, plus another 20,0 USD for delivery to the Floresti grain elevator;
- the Public prosecutor's office brought 8 criminal actions concerning violations revealed at Franzelutsa SA, and there were annulled dubious contracts of this enterprise with intermediary companies.

Are these actions enough? Do they guarantee that errors and abuses in the wheat and bread market, including those in which corrupted officials participate will not happen again?

Transparency and competition are necessary

As one can see, reaction of authorities to the wheat and bread crisis of 2003 showed mainly through administrative and organizational actions. But this is clearly not enough for transparency and competitiveness of the market environment.

Moldova's grain market tends to grow. Over the last years, more than 60% of sown areas have been under grain and in productive years export of wheat, barley and corn exceeds 1/3 of the total export of plant cultivation products. But there still has been formed no stable legal base of this market.

We already have exotic - for many other countries - laws "On wine" and "On walnuts", but no law on a more important thing - "On grain and grain market". Meanwhile, it is this law that - under experience of Russia, Kazakhstan, Ukraine, Romania and Hungary - has to be oriented at creation of legal, economic and institutional conditions for competitive production and formation of a grain market that would provide for the country's internal needs of bread, seed and fodder grain, as well as its export. The main aspects of the law should include: participants in the grain market, state support of grain production and processing, formation and utilization of grain resources, control over quality of grain, grain storage, organization of grain purchases for the state reserve, formation of an intervention fund to stabilize prices, grain export-import operations. Strict execution of such law will raise transparency and restrain voluntarism.

There are other actual problems that require solution. Will there be implemented a mechanism of state grain purchases from peasants on the security of their grain? Will standards of financial and informational service of the grain market be improved? How justified is preservation of the monopolist position of Franzelutsa SA in bread production? Why there were introduced no targeted compensations for bread for the poor instead of the populist, but unprofitable for the state, production of "cheap" bread for everyone?

All these solutions belong to the market arsenal. And unless we accomplish them, a bitter statement will remain topical: "Bad harvest of grain is a misfortune, but the rich one is a burden as well".

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[1] Íåò - ïîâòîðåíèþ õëåáíîãî êðèçèñà. "Íåçàâèñèìàÿ Ìîëäîâà", April 28, 2004
[2] Source: Department of Statistics and Sociology
[3] Government press release, July 6, 2004
[4] Ministry of Agriculture of Romania, AP Flux, July 8, 2004

Moldova - Transnistria: Rules for Business
Liliana Agarcova, 27 July 2004

Democracy and governing in Moldova
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A meeting of businessmen from Moldova, Transnistria and Gagauzia (Cocieri/Dubasari) was scheduled for early July. There have already been several meetings of this kind. They are held actively, but rarely - politicians hamper. The last of these meetings-discussions was held in Chisinau in November of 2003 at the initiative of the Centre for Strategic Studies and Reforms (CISR), the Small Business Association (Chisinau) and the Centre of Economic Studies, the Union of Manufacturers, Agrarians and Entrepreneurs (Tiraspol).

The motto was: "No word on politics, only on improving conditions for mutually advantageous collaboration". The parties agreed that by considering the interests of both business communities it would be easier to restore the integrity of the economic space, attract investors and large projects, jointly and proudly enter the external markets.

Recommendations were expressed, as well as the desire to form a consulting council for the authorities. But the "Kozak Memorandum" incident interfered. And the plans to meet again were thwarted by the recurrent burst of politicians' emotions, this time regarding the right to privatize industrial enterprises in Transnistria.

Fortunately, the life does not end here. And the search for common grounds to restore the integrity of the economic area of Moldova as a "common state" has to go on. More so, since the Republic of Moldova made several "steps forward" regarding registration, taxation, and protection of consumer rights.

Thus, so far, the problem of registration of economic entities from Transnistria at the State Registration Chamber of the Republic of Moldova and issue of papers confirming the place of manufacturing goods and services in order to apply VAT were the most spiny ones. However, the registration allowed economic entities from eastern raions of RM not to apply VAT on delivered goods and services, but it did require passing a series of bureaucratic procedures within tax and customs bodies and at the Chamber of Licensing. On the one hand, the provision on the registration of economic entities from the eastern raions at the Registration Chamber of RM in the Law on Enforcement of Title III of the Tax Code "Value Added Tax" may be seen as political, but on the other hand they may be seen as a tax concession upon delivery of goods and services, compared to those economic entities that are not registered. It is also important that the registration of enterprises from Transnistria has automatically granted a benefit to economic entities from the right bank of the Dniester, since the services they have received were not considered as imported and, therefore, the recipients of the services in Moldova were not obliged to pay VAT for these services.
More than a year passed since this novelty has been introduced (measures to carry out export-import operations by economic entities from eastern raions - that is the title of the decision of the Government of RM). And if at first it triggered negative reactions among Transdnistrian administration and enterprises, now the situation is totally different. According to the President V. Voronin, more than 400 economic entities of

Transnistria, including "Sheriff", have registered with the Registration Chamber of RM over the last weeks. What does this mean? One may assume that the decision to register was inspired by the economic benefits available. But it may also be related to the extension of the deadline for inclusion of Transdnistrian economic entities into the Moldovan State Register of Enterprises from January 1, 2004 to January 1, 2005? Or do Transdnistrian enterprises just bide their time?

Apparently, the issue of application of VAT on export-import operations of Transdnistrian enterprises has been settled, but it's not. Most likely, political considerations were decisive in deciding on the registration of economic entities from Transnistria, rather than economic ones. And Moldovan legislators, having disregarded the specifics of VAT taxation of services, automatically exempted Moldovan recipients of services from the left bank of the Dniester of VAT. After all VAT applied to imported services is paid by their recipients, with no right to offset paid VAT during the future delivery of goods and services. As a result of this decision, the state budget of Moldova had to "lose", while economic entities-recipients of services to gain.

And now, after a year, the Government of Moldova examines the issue of taxation of services rendered by Transdnistrian enterprises and it may well happen that these services will be considered as imported and their recipients will be taxed.

Since the business environment for the relations between economic entities of Transnistria and Moldova is still unregulated, discussions between businessmen might be of great help. And there are a lot of questions that require mutually acceptable solutions. Let us mention just the most important:

- Government of RM defined the tax policy for 2004-2007, which stipulates the reduction of the tax burden for businessmen and measures to support domestic producers, boost investments and export, small business development. Now, the Law on State Budget for 2005 is being drafted. It stipulates the reduction of income tax on business activity from 20% to 18% and income tax on natural entities - from 10% to 9%, from 15% to 14% and from 22% to 20% correspondingly depending on amount of income and increase of the non-taxable minimum of 3900 MDL per year for physical persons;
- In view of ensuring uniformed enforcement of the requirements of the Law on Procedure of Import to Moldova and Export from its Territory of Goods by Natural Entities, Customs Department of RM via its decision set a procedure allowing goods to be exported for commercial and production activities, if their value does not exceed 100 thou Euro. Goods that require licensing to be exported and strategic goods of double purpose are prohibited for export;
- Amendments to the Law on Customs Tariff reduce the term of reimbursement of customs duties on goods placed under customs procedure in the customs area from 30 to 10 days;
- Changes were introduced in the procedure of assigning tax codes, submission of data in cases when tax payer changes address, as well as procedures of replacing tax code certificates when lost;

- Amendments to the Law on Licensing of Certain Types of Activity provide for issuing a license for 1 year term for the activity related to gambling industry, 3 years term - for production of alcoholic beverages, 25 years term - for the activity related to production, delivery and transportation of electric power and distribution of natural gas;
- In order to create conditions for the activity of non-governmental organizations that are to get technical and financial assistance, the Government of RM issued a decision on assigning tax codes to these organizations located in the eastern raions;
- The Law on State Tax provides for a new type of duty to be levied for issuing licenses on the use of official or historical name of the state in a trade mark and/or service mark;
- The Law on Protection of Consumers' Rights bans import and delivery to the market of goods and rendering services if exhaustive and correct information is not provided in Moldovan/ Romanian and Russian;
- As part of Chamber of Commerce and Industry of RM expertise services on goods and contracts shall rendered to Transdnistrian enterprises.

A lot of time was wasted until Moldova and Transnistria finally came to an understanding that a joint agreement is to be worked out on the federative "common state". However, the process of reaching common grounds is difficult. Administrations agree and disagree, while the population and economy suffer. As long as both parties are close to a consensus on establishing a "common economic area", politicians and officials, rather than hamper contacts between businessmen should make use of their practical experience and initiative. We have to come to an agreement "for better is a neighbour that is near than a brother far off". And this Solomon's parable is 3000 years old.

Education - where is it heading?
Ion Basiul, 3 September 2004

Democracy and governing in Moldova
e-journal, II year, no. 36, September 3 2004

Drifting towards market economy, Republic of Moldova is confronted with numerous political, economic and social problems. Far from being encouraging, especially given the worsening situation in education, which after all is the main pylon of the human development in Moldova.

The conflict around the Moldovan Latin script schools in Transdniestria has made things even worse. It was triggered by Tiraspol secessionist regime. Despite the efforts of various international organizations to settle the conflict, the situation around the six schools in Transdniestria remains tensed at the beginning of the new school year and it seems there is no way out.

In a related note, things are not so rosy on the Moldovan side either. Massive exodus of labour is gaining grounds, and great many of them are teachers. According to a UN report, in the last ten years 48,000 teachers have left their job in search for a better wage and therefore a better living abroad. And the reason for that is the slow pace of salary raise as compared to the cost of living and as compared to other sectors of economy. Another illustrative figure, average monthly wage for a teacher this year, 660 Lei, represents only 61% of the average wage per economy (1 USD ~ 12 Lei). Average wage of a professor, 880 Lei, represents 93.5% of the average wage per economy.

Annually Ministry of Education sends around 500 University graduates to the schools of the country, out of which almost a half quit their jobs and flee for a better life abroad, or try their luck in other sectors where they could count on better wages. Around 600 out of the 2,000 graduates of pedagogical institutions sent to schools and lyceums stayed with their job. The shortage of teachers last year reached 1,300 people, while currently there are 22,441 vacancies in schools only.

Recently Government passed a draft on amending the Law on Education aimed at attracting young graduates to schools in rural areas. Under the draft, graduates of pedagogical schools shall be entitled to a single indemnity equal to four minimal salaries, whereas graduates of universities to six minimal salaries. In addition they shall be entitled to bonus equal to 50% of the minimal salary in economy and a series of other benefits that would supposedly lure graduates to rural areas. Of course Government undertakings are worthwhile, however the draft provides no benefits to the teachers already working in the field, on top of that 2004 state budget does not provide for any salary increase in education.

Yet another problem is the situation of the retired teachers. There are teachers who worked for 30-40 years in schools and now get a meagre pension worth 300-400 Lei.
In a related note, one may only applaud Government's actions towards adopting Code on Science and Innovation, despite the flaws and criticism voiced by opposition and ruling party alike. In the eyes of many it should not be called a Code at all, as codes

apply exclusively to legal fields. Others, oppose the Chairperson of the Moldovan Academy of Science to seat in the Government.

As previously mentioned, education in Moldova faces some major deficiencies. Signing Cooperative Agreements with various international educational institutions would likely improve the situation in the Moldovan education system. In this respect it is worth mentioning the moral and financial support provided by Romania, which annually grants scholarships to young Moldovans in various fields and offers high-quality education. There are high expectations that once they get familiar with Western experience when returning home young Moldovans would help the country take its due place among other developed countries.

Energetic dependence
Iurie Gotisan, 3 September 2004

Democracy and governing in Moldova
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For a while now the energetic sector that is of vital importance for the economy has become a battle field where political and economic interest collide. On the one hand, there is a struggle between domestic players in the field, and on the other there is an increasing pressure from several Russian companies seeking to extend their spheres of economic influence in Moldova, both via acquisition of assets as well as involvement in production, delivery and regulations in the energy sector. This specifically refers to Russian Gazprom, the world leader in the field, having an annual output of around 500 billion square metres.

Noteworthy, currently EU economy imports 52% of its energy, however by 2020 the enlarged EU (30 countries) would import 78%. Oil and natural gas are of key importance. Growing gas consumption in Europe in the next two decades would be almost totally covered from Russian exports, which would double to EU. There are plenty of examples in history when such a heavy reliance on imports from one single country was exploited by that country as a virtual means to wield pressure or exert strategic political threats. Hence, in the last 30 years various oil crises, regional conflicts and errors in domestic energy policy have been quite illustrative of the strategic and political importance of energy source.

Even if EU has sufficient "currency" to counterbalance its ties with Russia, Central and East European countries, including Moldova, are far more vulnerable, whereas the pressure they face is far from virtual but rather more straightforward. When you are not under the strong EU club umbrella and don't have at least a square meter of gas in your land, and the bill for consumed natural gas exceeds by far the national budget, gas supplier (in our case Gazprom) should be duly rewarded in political, diplomatic or commercial currency. In the last decade there were numerous incidents when the gas supply was cut, back then Russia was not the only bad guy, but also Ukraine on whose soil gas transits.

Unfortunately one has to acknowledge that economic independence of Moldova is a nice dream. Being aware of the key importance of gas in ensuring Moldova's energetic security, Moscow managed quiet easily to turn it into a tool for wielding pressure on Chisinau domestic and foreign policy. Moldova's dependence stems from two facts. Firstly, the lack of own resources that may be explained by geographic factors and equally so by dependence on a single source of imports, namely natural gas from Russia. Secondly, a more dangerous one - debts. According to official statistics, Moldova's total debt on natural gas supplied by Russian Gazprom, including the penalties, is estimated at 300 million USD, whereas Transdnistrian debt exceeds 1 billion USD.

At the same time Government is not actually trying to change this state of affairs, which may lead one to the conclusion that energy imports from Russia to Moldova are more than mere "import" that cannot be explained by the strive to maximize the profit. In the case of Moldova, widening its berth for manoeuvres is directly proportional to swelling debt on gas supplied by Russia, which conditions debt payment by participation of its companies in the privatization of Moldovan companies. The fight for companies in energy sector has become an economic and political affair due to strong lobby campaigns undertaken by each of the individual players. After all it is quite clear why political reasons take over economic ones.

This also explains Russia's tolerance towards Moldova's huge debts, as political gains in the long run may well compensate net present value. Moldova's passive energetic policy may enhance even further the negative consequences in case Russia puts "energy weapon" in use. Chisinau does not try to go one step ahead and anticipate changes in the bid terms, nor does it attempt to make an order in its relations with Transdnistria, diversify its suppliers, or change the archaic and high energy consuming industry and public sector. In fact Moldova turned into an attachment of the Russian energy policy, not even having an active position at the negotiation table. Unless Chisinau energy policy improves, in the near future Moldova's dependence on Russia would further increase.

In this respect, the relations between Ministry of Energetics, Moldova-Gas, Union Fenosa and Moldoelectrica have become quite tensed. Nothing of this would have happened if Moldovan-Russian negotiations on debts payment had not been held behind closed doors, and if relations between companies on the market and regulatory institutions on the market had been ruled by the law rather than telephone calls. Furthermore, recent escalation of the conflict between regulatory agencies (Ministry of Energetics and National Agency for Regulation in Energetics) is yet another weak point on the market. The conflict was triggered by the cut-offs of electricity in many localities of Moldova by Cuciurgan Thermoelectric Station. It is known for a fact that it is operating on natural gas supplied by Gazprom and is controlled by the Tiraspol secessionist regime, which in turn is loyal to Kremlin.

Shortly after the "show" was over, another actor showed up on the scene, i.e. coming directly from Moscow the Deputy-Chair of Gazprom, Aleksandr Reazanov. His company together with RAO ES have never made a secret out of their interest to control energy export to the Balkans. Russian dignitary stated at the meeting with Moldova-Gas leadership that Russian Federation was ready to restructure Moldova's debt on natural gas for another five years. By tolerating Moldova's impressive bills, Russia seeks to secure political attachment from Moldovans towards Russia.

Nevertheless, Chisinau has made no effort to find a solution. Moreover, it has undermined even the modest undertakings of the previous governments to increase imports from Romania as well as to diversify import sources, like from Romania and Ukraine. There is no excuse for the Chisinau's refusal to Bucharest's initiative to finalise together the construction of Cernavoda atomic station that would have entitled Moldova to energy produced at one of the reactors. Albeit very advantageous for Moldova the proposal was declined. Of course it would have required an investment from Moldova, however in the long and mid term these would have been worthwhile.

Restructuring state enterprises in the thermo-energetic sector would be one alternative that would allow reducing costs on raw materials. Because of high production costs and obsolete equipment the latter are the greatest gas consumers and the main Moldova-Gas debtors. A reminiscence of the soviet-type mentality, freezing debts swells the budget deficit even further, as well as total debt to energy suppliers, mainly Russia. Private consumers account for only 20% of the gas consumption which as a rule is paid on time. If those measures are taken they would reduce debt burden and bring relations between Moldova and Russia from political to economic dimension. Moldovan politicians should consider a quite interesting fact Central and East European countries are as much dependent on energy imports from Russia.

Chain reaction triggered by skyrocketed prices on fuel
Iurie Gotisan, 8 September 2004

Oil price that hit its highest induced a price hike on fuel and diesel this year. Fifty dollars a barrel may not leave Moldovan market indifferent. Drivers would be the first one to feel on their own the short-term effects of the price hike, followed by all businesses where fuel accounts for the great part of the final cost, or where it is used as a raw material. Private transportation companies have already increased the fares for passengers. However the price hike would be even bigger in the case of goods transportation. Also, prices on food and beverages would likely be propelled further upwards; however such a decision would be taken by the manufacturers in the moths to come. Bread and bread products would be an exception as the low price on grain would likely compensate the price hike on fuel.

Goods transportation would be directly affected by price hike on fuel. Recent price "adjustments" on fuel by petrol stations, have propelled prices on diesel further upwards, which translates in higher costs for transporters. Diesel has increased by 6%, which translates in a 2% increase in costs if we are to consider that on average it accounts for 20% of the expenses. Operators shall bear only a part of the additional expenses, while consumers the rest. There are also some efficient transporters where fuel accounts for only 15% of the costs. In their case, price hike may represent only one percent of the actual tariff. Of course there are also inefficient transporters where fuel accounts for 30% of the operational costs. The prices on the domestic routes knew a modest increase, whereas on international ones price hike would have a considerable impact on cost. Therefore, it is to be expected that eventually transporters would swell the price on international goods transportation. This would lead to fierce competition, while players would loose in competitiveness.

According to government officials, supposedly a good agricultural year would counterbalance the price hike so that it does not affect inflation. However, keeping down the price on bread is far from enough to keep the inflation in the forecasted limits. Experts say the price on bread would not change even after fuel prices rose. As the bread factories purchase cheaper grain, the price hike on fuel shall be compensated by the low price on the raw materials. On the one hand, a considerable increase in prices is to be expected in two or three months upon the end of production cycles that are now working on a more expensive fuel. On the other, most likely producers would internalize those costs for fear of eventual drop in sales in case prices went up. Later on, most likely the diary products would follow. Additional expenses on transportation would show up in two months or so, when manufacturers would likely swell the prices by 10%. This would also include diary products. A 4-5% increase in vegetal oil price is expect this fall due to poor harvest this year and the same price hike on fuel. Following the same partern packaging price is also set to soar. On top of that, price hike lays the economic and psychological grounds for further increase in prices on other food.

In the end price hike on fuel would boost inflation. It is not the only factor to pose a treat to the forecasted 10% inflation rate, but also swelling bills on energy and gas as was recently announced by Union-Fenosa and Moldova-Gaz. Despite the warnings of many experts, it is said that inflation is set to soar only next year, as in 2004 growing price on fuel is to be compensated by low prices on bread. For the state budget, swelling fuel price is not necessarily a bad news as it means more excises. In fact, increased excises on fuel coupled with growing imports boosted the nominal value of revenues from excises by 40.1% over same time 2003. However growing oil quotations and imports far beyond expected ones are affecting the current account deficit. To diminish the effects of the high price of oil imported in the country, Government may want to lower the excises and abolish VAT on excises. However, so far Government is not even considering this possibility.

Oil quotations on the world markets

Both events in Iraq and problems surrounding Russian giants YUKOS and TRANSNEFTI have led world markets into believing that end of August would mark an oil crisis. Numbers have scared many investors. Even if oil hasn't hit 50 USD a barrel, still two weeks ago it was quite close, with 49.40 USD, the highest in 21 years. Now there is a 40% increase over early this year when quotations neared 32 USD a barrel. The chances that there would be a considerable drop in the near future are very slim given the ever growing demand. Only China's imports, the second largest importer after US, have surged by 40.7% in July over last tear, whereas India is expected to import 11% more in 2005 alone. OPEC countries have little if no spare capacity. They supply 30 million barrels a day.

Oil price race has raised worries in great many countries. For instance Japan's Ministry of Finance has already started monitoring its effect on the country economy, whereas American Federal Reserves took similar measures while keeping silent on whether it would affect economic recovery. Reserves are plunging in US, amidst a 3.4% surge in demand which fully covers imports from OPEC countries, Saudi Arabia in particular. Oil quotations have started going down last week once Iraq resumed exports, which calmed down fears of an oil crisis.

Both US and European stock markets were affected by strife-torn Iraq and high oil quotations. After oil price race sent stocks down, falling oil quotations have now sent the stocks up. Experts say that a new oil price surge is unlikely, except for cases when market fears over an eventual crisis would turn real. There is a growing optimism fuelled by clearing situation in Venezuela, stabilization of Iraqi exports and positive signs from YUKOS.

Recent State Initiative on Land Consolidation
Felicia Izman, 15 September 2004

Democracy and governing in Moldova
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Since its coming to power in February 2001 the new Moldovan communist leadership has often expressed its nostalgia for the old times of collective-type agriculture and criticized the National Land Program (NLP) that dismantled this system by creating a private-based agriculture sector with hundreds of thousands of new individual land owners and thus a highly fragmented one. The first policy proposals on administrative-type land consolidation and creation of production cooperatives had been unveiled in mid-2003, but concerted pressure from major donor organizations had forced the GOM[1] to retract these initiatives.

The second attempt, in a more explicit form, came out in January 2004 in form of two legal documents "The State Program on Agricultural Land Organization and Arrangement" and "The Law on Agricultural Land Organization and Arrangement". A revised (more focused and detailed) draft version of these documents was then released in mid-April 2004 and circulated among various ministries. As of today, no final document on this highly controversial issue of land consolidation has been approved yet.

The released documents, particularly the State Program (SP), call for embarking upon a major sector restructuring through encouraging the creation of "consolidated enterprises" (basically production cooperatives). The implementation mechanisms described consist of a series of wide-ranging actions including redrafting of major laws, creation of new commissions and adoption of tax, pricing, crediting, marketing and land policies. The documents also call for elaboration of a new Land Code that "would serve better the needs of the sector in the present post-privatization phase" (quotation from SP). Such a code is currently under elaboration within the Ministry of Agriculture and no draft has been released yet.

According to the draft SP, the GOM's reasons for undertaking land consolidation are based on a number of key assumptions that: (i) land fragmentation that occurred as a result of NLP is currently excessively high in Moldova; (ii) individual agriculture is inefficient and uncompetitive; (iii) only optimal-size consolidated agricultural enterprises will be able to produce a high-quality and competitive output; and (iv) creation of consolidated enterprises will create new jobs, increase labor productivity and stop the population outflow from the rural areas.

A rough analysis of these key assumptions easily reveals their un-sustainability and false nature. First, regarding the claimed high fragmentation of agricultural land, we shall take a look at the statistical figures that disclose the following picture of agricultural land tenure in 2003: 54% of the total land fund distributed during the privatization period is currently utilized by relatively large-scale corporate farms (mainly LTDs, but also production coops and joint stock companies) that have in use between 100 to 1000 ha. It is therefore clear that the quickly emerging land lease markets have already resolved to a great extent the fragmentation problem and will continue so as the land market develops further. The second statement with regard to the inefficiency of the individual agriculture is totally wrong provided that today the individual sector[2] produces as much as 75% of the total agricultural output by the use of only 56% of total agricultural land, thus exhibiting a significantly greater productivity than the large corporate sector.

The third assumption stating that only consolidated enterprises would be capable of producing a competitive and high-quality output can be easily refuted by the evidence of the mid 90s when the existing kolhozes and sovhozes were loss-making bankrupt entities that kept accumulating more and more debt every year. It thus seems that the GOM proposes to solve the issue of rural poverty by returning to a failed economic system, which was unsustainable in the past and will certainly be so in the future.

And last but not least, while the creation of consolidated enterprises may initially create some new jobs (which shall not be a goal by itself in a country with half of the population involved in farming!), it is not at all clear how this would contribute to labor productivity growth, as according to the laws of economics it would rather do the opposite: the inflow of new labor would only worsen the already low labor productivity indicators of the Moldovan agriculture sector. Moreover, it would certainly not stop the population outflow from the rural areas for the simple reason that these enterprises won't be able to pay a wage anywhere close to the competitive wage range. What would really improve the standard of living of the rural population is the opportunity for people to find jobs outside the agricultural sector, which would ensure labor outflow from the sector, thus contributing to both land and labor productivity growth in agriculture. So, focusing on the real problems of the agricultural sector, such as the underdeveloped markets and services, as well as finding ways to develop and expand the non-agricultural part of the Moldovan economy should actually be the major GOM's concern nowadays (see also Box 1).

Box 1. From the Economist Intelligence Unit (EIU) "A backward step for agriculture":
"Assuming that the CPM administration proceeds as planned, the results are almost certain to be negative. The CPM's program reflects its ideological antipathy towards private agriculture, and the solutions it offers stem from a misdiagnosis of the agricultural sector's problems."

It is therefore obvious that under false premises the GOM tries to drag the individual agricultural producers into some-type of collective enterprises that clearly proved their un-sustainability under market conditions in the mid 1990. The draft documents foresee very facilitating procedures for creation of such a consolidated enterprise by requiring the consent of landholders that own not more than 2/3 of a land tract (which by the way means the rest will have to comply against their will). By contrast, the exit procedures seem much more complicated if not impossible, since "the consolidated enterprise breakdown is prohibited if this resulted in size reduction under the minimal optimal level[3]". This is a clear violation of the constitutional property rights of land owners. A stipulation that clearly unveils the control-driven nature of this political initiative is that "the consolidated enterprises are to be run by specialists appointed by a rayon-level commission".

A recent study[4], which attempted to spot farmers' attitude toward this land consolidation idea found that 76% of landowners/lessors and 82% of lessees would not agree to transfer their land to a consolidated enterprise. Typical reasons given for not wanting to do this were "won't be able to pass my land over to my heirs", "the collective farm will not be more efficient and the employees will be irresponsible", "can sell my land anytime now", or "am satisfied with my land lease contract".

It is thus a pity that the GOM, blinded by its short-sighted political motives, does not want to see the long-term negative consequences of such disturbing policies, including the worsening of the investment and business environment due to insecure property rights, an even further drop in the currently depressed private investments, reduction of external financial inflows, etc. Luckily, it is not at all clear how the Government will get hold of the necessary resources to finance this costly program estimated at 70-90 million lei ($6-8 million). According to EIU, "this represents the best hope by far for preventing its implementation, given that the government is effectively broke." External donors will most probably not show eager to provide

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[1] GOM - the Government of Moldova

[2] The individual sector is comprised of peasant farms and household plots

[3] A precise definition is provided in the draft law for the minimal optimal size of a consolidated enterprise, which is: for crops - 100 hectares for cereals and technical crops, 10 ha for orchards, vineyards and vegetable plantations, 1 ha for berries, strawberries and greenhouses; for livestock - 15 dairy cows, 50 cattle, 100 hogs and 2000 poultry

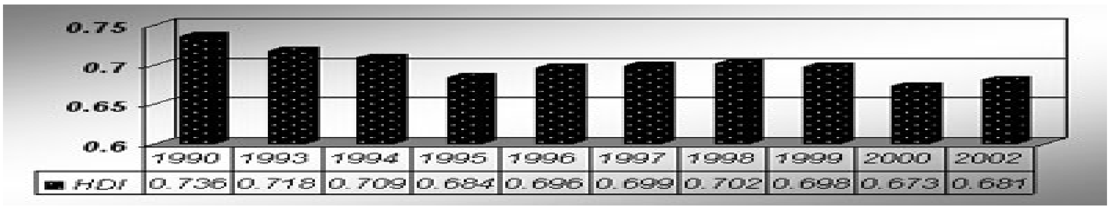
[4] "Lease of agricultural lands - 2003", CISR/PFAP, Chisinau, December – 2003

Economic growth does not connote higher human development
Ana Sirbu, 20 September 2004

After a two-year pause, a fresh Human Development Report of Moldova was finally launched in the end of July. Its theme was *Good Governance for Human Development*. It has been determined that there is a strong direct correlation between the level of good governance and that of human development (HD) in a country. The topic elected has proved to be a very audacious one, as characterizing, analyzing and proposing potential measures for a country's governance is not an easy task.

HD is the fundamental goal of the humanity. It is the process of enriching the spectrum of human opportunities for the people all around the world. It permits and facilitates the accomplishment of beautiful, long, healthy lives. Although the human development index (HDI) does not provide us with an exact, irrefutable measure of the HD level of a certain country, it certainly gives us a good picture of where we stand among the other countries of the world in terms of income, health and education. Moldova is placed on the 113th position among 177 countries rated in the yearly Global Human Development Report, pertaining to the category of the Medium HD countries. Although Moldova was in the first half of the 90's one of the most progressive post-soviet republics in terms of reforms, it has not managed to even slightly maintain the position it had in 1990 when it was ranked on the 64th place according to its HDI. Since then, the human development level of Moldova fell drastically. Now, 14 years later, the republic's position is almost twice lower among the countries of the international community.

Our attention is caught by the fact that even after four years of steady economic growth: 2000-2003, although our GDP continues to rise, the HD level of the country does not ascend.



The HDI evaluates the general accomplishments in a country in terms of three basic aspects: longevity (life expectancy at birth), knowledge (adult literacy rate and combined enrolment ratio), and a decent standard of living (adjusted per capita income in Purchasing Power Parity-PPP$). This year's global report determined that, in 2002, Moldova was on the 113th place, with an HDI of 0.681 on a 0 to 1 scale.

There are three groups of countries according to their HD level: high HD: HDI>0.8; medium HD: 0.5<HDI

Now, more than 60% of the world's countries have a higher human development. Moldova is one of the Medium HD countries. But unfortunately, in the transition period, Moldova has had almost the lowest rhythm of economic growth (besides Tadjikistan) amongst all the ex-soviet republics

Although the country's GDP has grown by a total cumulative of 24.1% for the period 2000-2003, when economic growth was finally renewed, its HD position is that same 113th position as it was in 1995, after the sudden transition shock, when the country just started implementing market reforms. Comparing the data used to determine the HDI in both 1995 and 2002, we can analyze the structural changes this index experienced. Considering the components of the HDI in both those years, we are able to see in which areas the Republic of Moldova became stronger and which ones we regressed in. We can observe that life expectancy at birth increased by one year (from 67.8 in 1995 to 68.8 years of age in 2002), despite the high level of poverty and the low level of accession to healthcare by the financially vulnerable segment of the population.

In the education domain though, the situation worsened considerably. The adult literacy rate dropped by 8.9 points (98.9% in 1995 and 90.0 in 2002), and the combined first-, second-, and third-level gross enrolment ratio decreased by 5 points (from 67% in 1995 to 62% in 2002). Why is now almost 9% more of our population illiterate? A large number of people cannot afford education, not even first- and second- level education that is public and free. A large number of children are obliged to work within their households and later, instead of attending the University a lot of them chose to work, within the country or abroad. Although the total number of learning institutions in Moldova is now higher (1674 institutions in 1995 and 1778 in 2002), the total number of students pursuing their studies within these institutions has decreased: 766.5 thou in 1995 and 738.1 thou in 2002. Besides this, our population is steadily decreasing (4.34 mil. in 1995 and 4.23 mil. in 2003) and instead of the elderly people who had received an education, appears the new generation that is not too much aware of the importance of learning. A number of qualified workers, teachers, doctors, etc. leave the country and the schools remain without the employees it once had. Sending their remittances home, all these people contribute to a higher GDP of their country, but a higher GDP does not mean a higher human development level.

In Moldova, the GDP per capita grew indeed between 1995 and 2002, a change confirmed by the increasing *GDP index*: from 0.23 in 1995 to 0.45 in 2005 and the increasing *real GDP per capita (PPP$) rank minus HDI rank index*: from 23 in 1995 to 36 in 2002. Since the remittances sent home continue to increase, these numbers will most probably augment as well. However, we remain on the 113th place. According to the Department of Statistics and Sociology, Moldova is among the countries with a low level of income ($543 for the year 2003). Thus, if not for the remittances sent home by the people employed abroad, it would be a paradox that, with such low incomes, consumption is so pervasive and accounts for more than 100% of the country's GDP. The per capita income in Moldova also speaks about our current poverty situation: circa 40% of the population is below the poverty line. The income insufficiency and the income unequal distribution (the Gini coefficient was 0.421 in 2002) trigger a lower level of healthcare and a worse attitude toward education. Therefore, in order to reach a higher level of human development, the best has to be done in order to eradicate poverty.

We still have a long way to go. In the high human development countries, the average life expectancy at birth is circa 10 years higher than that in Moldova. Education dropped in Moldova, and enrolment in education institutions decreased (this percentage being of only 62%, compared to the high 80's and low 90's percentile of the highly developed countries). Therefore a higher attention has to be given to both healthcare and education.

Although we still are among the countries with medium Human Development, Moldova's position on the HDI ladder has significantly dropped since 1990. Poor education and healthcare are fully recognized signs of poverty, thus the best has to be done in order to eradicate poverty. Also, not only Moldova degraded since 1990, but the other CIS countries proved to be capable of a much sharper and effective progress. The HDI offers us information not only to know how developed we are in comparison with the other countries of the world, but also enables us to deduce a number of conclusions regarding the development dynamics of Moldova relative to other countries and the fields in which a number of measures need to be taken in order to improve our level of HD. It shows us the countries that progressed, that could give us an example of reforms the implementation of which was proved to be effective. Economic growth certainly helps, but it does not necessarily connote a higher HD level.

Indebtedness threatens the stability of domestic economy
Iurie Gotisan, 29 September 2004

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As in many other transition economies, in Moldova there is a huge difference between state-owned and private companies when it comes to honouring obligations to the state budget. To put it differently, fighting arrears should be backed up by imposing budgetary restraints so that companies (especially state-owned ones) pay taxes to state budget. Having said that, last week Government's ordinance on cancelling debts worth 107.5 million Lei (http://www.azi.md/news?ID=30915) incurred by a number of agricultural companies, is yet another illustration of the differentiated approach. The thing is there is a clear case of discrimination of private companies not entitled to fat benefits against state-owned companies that are.

The draft law developed by the Ministry of Agriculture and Food Industry and endorsed by the Government provides for writing-off the debts to the state budget (as of January 1, 2004) for 30 agricultural entities, great many of them sovkhozs, kolkhoz and production cooperatives. Furthermore, the draft obliges local government to take "measures in the next years in view of totally or partially writing-off historic debts incurred by the economic entities subject of this law". No wonder the list of those entities was never made public, nor were details of the would-be writ-off; however one may only guess who would be the lucky ones. Indeed, this draft law would prove quite handy to moguls in Government or Parliament, who are in fact behind those entities.

Probably, officials refrained from making public the data not for the fear of westerns, but rather for fear of their own people! It comes as no surprise that Communist ruling has made keeping secret or even distorting data a daily business. Specifically, information impossible or not advisable to hide was "cosmeticised". Writing-off arrears as well as restructuring state-owned companies' debts may ruin all official forecasts on inflation, say analysts. To give just an example, according to Sociology and Statistics Department inflation rate for the first half of the year was 13.3%, Republic of Moldova ranking the second after Belarus (20.3%) among CIS countries as regards rising pattern for inflation. Experts claim the psychological threshold of 10% inflation rate would never be reached, unless of course "official data are falsified". Officials though stay calm and see no harm in soaring debt.

No one could asses precisely the impact of those write-offs and restructuring, as nobody works seriously on economic models in Moldova and there are no sufficient statistics (there are even some gaps). Having said that, authorities are walking in darkness when making their economic forecasts. In the end inflation rate is much lower in the statistics than in the peoples' pockets, as is economic growth much more significant than the one felt in economy and state budget. On the contrary, "disturbing" data not included in the obligatory reports were simply forgotten. Still, what happened with data on arrears per economy was far too much. Communist Party 2001 governing program pointed to the dangerously high arrears incurred during the previous rulings, claiming that they had reached 30% of the GDP in 2001. Hence, data related to arrears are classified. Not even annual reports of the Ministry of

Finance were published, not even an official estimate of the arrears was released. The reasons are easy to guess: during the incumbent ruling arrears continued to grow and probably at a faster pace than before! If they had dropped, the data would have been made public long ago and listed under new governing "achievements".

Normally, during incumbent ruling arrears continued to soar due to some objective as well as subjective factors. On the one hand, a string of constraints from outside imposed either a massive restructuring, or pushed suppliers and state to go for non-payment. Companies have chosen the second, especially as there was a political consent to that. Banking sector restructuring shut the doors to bank financing for bankrupt and inefficient state-owned enterprises. On the other hand, never was the state more tolerant towards non-payment of financial obligations. All kind of schemes for restructuring debts, providing additional benefits, or even writing-off historic debts provided current debts were paid, have been put in place. Noteworthy, last week Government together with the State Creditors Council passed a resolution on restructuring historic debt to state budget for two CET (thermo-electric plants) worth 187.5 million Lei. Moreover, one month ago Government and State Creditors Council froze the historic debt of seven tobacco companies worth some 25 million Lei.

Worryingly, manufacturing based on indirect financing was encouraged, namely from fiscal credits (non-payments of obligations to public budgets) or from state aid (non-payment of financial obligations by state-owned energetic units). Never bad debtors enjoyed such a heaven having a political blessing from the top. All of the aforesaid propelled the arrears to public budgets further upwards (that were turned into heaven for tax dodging), as well as to energy suppliers, which being state-owned were not allowed to cut supplies to bad-debtors.

One year ago, total arrears per economy were 4.5% higher over the end of 2001, i.e. 200 million USD, according to IMF report. Anyway, out of the total arrears estimated at 30% of the GDP, budget arrears do not account for more than 3%, according to the Ministry of Finance. On the contrary, scoring high after arrears to public entities are arrears to public budgets, in which bad-debtors found the perfect loophole.

High rate of bad-debts has determined banks to raise interest rate. Noteworthy, even though a growth of industrial output has been registered in the last two years, cross debts among business plus debts of the latter to commercial banks is estimated at 4 billion Lei, i.e. 14% of the GDP in 2004. Excessively high rate of bad debts in financial institutions undermines economy, whereas the level of obligatory reserves, an instrument used by National Bank to control liquidity, raises the cost of commercial banks, thereby making crediting of real sector more onerous. On top of that, the cost of a credit in national currency is more expensive, and this amidst over-appreciation of national currency that neglects its real value. This is why other than governmental credits in foreign currency show signs of growth and according to National Bank amounts 200 million USD.

As of August 1, companies' debt to consolidated budget reached 1,059 million Lei (88.2 million USD) a 9% increase (87.5 million Lei) since early this year, reads a press release of the State Fiscal Department. Bad debts account for 72% of the total debt. Bad debtors include businesses that are not operational for more than three years - 226 million Lei, litigating businesses - 102 million Lei, bankrupt businesses - 97.5

million Lei, as well as businesses having no assets - 100.7 million Lei. Thermo-energetic sector owes another 228 million Lei to the consolidated budget.

However governmental program does not refer to areas to state budget. It envisages decreasing new arrears that annually add up 4% of the GDP to the historic arrears. The latter more or less equals the amount public budgets and entities are supposed to get. By reducing "historic" debts one does not really diminish the arrears. One might only diminish them by reducing new debt that adds up. In this respect, Ministry of Finance failed to honour its obligations. It comes as no surprise that IMF opposed Ministry of Finance initiative to use additional budget revenues coming from economic growth for social spendings. If not for other things, at least IMF has the merit of disclosing figures and actions authorities remained tight lipped about. Finally, if freezing debts shall not be accompanied by payment of current debts, in a year or so Moldovan economy would be on the verge of collapse, while the debt burden would be so great that it would likely suffocate state budget and private sector.